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Montana Lottery

FY 1999 Annual Report

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The Montana Lottery is pleased to present its Fiscal Year 1999 Annual Report. The Montana Lottery is a business, with a main goal of raising revenue, like other businesses in the state. The difference between the Lottery's mission and those of other corporations is that, to some degree, everyone in Montana benefits from Lottery sales and profits. Since its inception 12 years ago, the Lottery has contributed more than $79 million to the programs the Legislature has designated.

The success of the Lottery depends on the confidence citizens have in the integrity of our operations. Along with this integrity emphasis, the Lottery staff and vendor partners look for innovative ways to operate the Lottery more efficiently, while increasing sales, expanding services and keeping up with the latest technologies.

In fiscal year 1999, several events were of note. First was the inception of a seven-year contract with our new On-Line Vendor, Autotote Lottery Corporation. Our new contract went into effect March 28, 1999, with the installation of our new *Probe*L* on-line terminals, and Instant Ticket Validation Terminals across the state. With any computer system conversion come inevitable problems, but thanks to the tireless efforts of Autotote, Lottery staff, and our retailers, we have reached acceptable system operations. However, there is and will be a continued effort throughout the contract to improve this computer system.

On the eve of our on-line conversion, a Montana Lottery ticket was sold which matched the winning Powerball numbers. Dean and Kristi Drenzek of Glacier become Montana's fifth Powerball jackpot prize winners, claiming a $19.3 million dollar cash jackpot. This young couple, teachers in Browning, did not claim their prize until early June, choosing to wait until the school year ended to minimize the disruption to their students and their community.

Another highlight of fiscal year 1999 was the continued growth in Scratch ticket sales. Scratch sales increased three percent over fiscal year 1998. Along with this increase came an increase in total operating revenue, up one percent; and total transfer, up three percent from last fiscal year. This is the second year in a row the Lottery has seen an increase in both ticket revenue and total transfers.

We look forward to the future. With improved technology, the hard work of our staff and vendors, and the constant support of retailers and players, the Lottery will continue to provide benefits to all of Montana.

Sincerely,

Gerald J. LaChere

Director's Message

Gerald J. LaChere

Becky Erickson, Chair, Glasgow

The Montana Lottery Commission is composed of five members appointed by the Governor. By law, one member must be a law enforcement officer, one must be an attorney licensed to practice law in Montana, and one must be a certified public accountant. Among other responsibilities, the Lottery Commission, in conjunction with the Director, is charged with setting policy for operation of the Lottery, determining types and forms of lottery games, ensuring the security and integrity of the Lottery, and maximizing revenue paid to the State. The members are appointed to staggered four-year terms.

The Montana Lottery Commission is pleased with the Lottery's successes this past year. In addition to posting a slight increase in both operating revenue and total transfer to state programs, Director LaChere and his hard-working staff weathered a complete on-line system conversion, while continuing day-to-day operations required to run the multi-million-dollar operation that is the Montana Lottery.

The Montana Lottery Commission as of fiscal year end 1999 consists of: Becky Erickson, Chair, Glasgow; Clifford Brophy, Columbus; Tom Keegan, Helena; Carol Thomas, Great Falls; and Robert Crippen, Butte.

Lottery Commission

1986

November 4 – Legislative Referendum 100, the Montana State Lottery Act, passes by 67 percent of the popular vote, carrying each of the 56 counties. Lottery profits to go to Teachers Retirement Fund for the purpose of holding the line on or reducing property taxes.

1987

June 24 – First instant game, *Pot of Gold*, goes on sale.

July 15 – Premiere of the first Big Spin TV Show, 30-minute special. $26,000 is awarded in cash prizes to seven lucky finalists.

1989

August – Montana Lottery launches its first merchandise Scratch game, *Pickup Plenty*, which features a top prize of a 4X4 pickup, along with cash prizes.

November 9 – *Lotto*America*, a 6/54 Lotto, two-draw per week game, goes on sale in Montana.

December 28 – The last Big Spin Show. 460 finalists share in total winnings of $7,730,000.

1990

April 4 – First Big Win event, Missoula. Ten finalists share $205,000 in prizes.

July 1 – Legislature changes where Lottery money goes—from the Teachers Retirement Fund to the Office of Public Instruction School Equalization Account.

September 12 – Final Big Win show in Billings.

1991

May 6 – First day of sales for Montana's 5/37 game, *Montana Ca$h*.

July 1 – By Legislative action, 1.6 percent of Lottery profits are now transferred to the Board of Crime Control to fund administrative costs associated with juvenile detention centers in Montana.

1992

April 19 – *Powerball* sales begin. The multi-state game replaces *Lotto*America* and offers nine ways to win, improved overall odds, and a larger jackpot.

April 22 – First *Powerball* drawing. Montana also adds a second weekly drawing for *Montana Ca$h*.

July 1 – A larger portion, 9.1 percent, of the Lottery's profits are now transferred to the Board of Crime Control.

1993

February 26 – First drawing for *Tri-West Lotto*, a 6/41 lotto game offered with Idaho and South Dakota.

March – The Montana Lottery introduces a multi-game Scratch concept to retailers, introducing a new game every month.

1994

February 4 – First drawing for the revamped *Tri-West Lotto*, which was reintroduced as a 6/33 game, with improved odds of 1 in 17, an all-cash jackpot, and set prize payouts on low-tier prizes.

March 1 – First *Bingo* Scratch tickets go on sale, Montana's first $2 game.

July 1 – By Legislative action, all proceeds of the Montana Lottery are transferred to the State of Montana General Fund which funds the general operation of the state.

1997

February 4 – Montana Lottery introduces an Instant Ticket Validation and Accounting System and nine new Scratch games.

May 12 – Montana Lottery introduces *Daily Millions*, a daily on-line game featuring a chance at winning $1 million cash every day.

June 24 – Montana Lottery 10th anniversary.

July 1 – By legislative action, up to $100,000 over fiscal years 1998 and 1999 is transferred to fund a study on the socioeconomic impacts of gambling.

November 2 – *Powerball* game changes. Starting jackpot increases to $10 million. Players can choose a lump sum cash amount at approximately half the estimated jackpot or a 25-year annuity.

1998

February 1 – The Montana Lottery introduces *Wild Card*, a 6/38 game, and discontinues *Tri-West Lotto*. The game is also offered by Idaho, South Dakota, and Nebraska.

March 30 – *Cash 4 Life* is introduced in Montana and ten other lotteries. The game replaces *Daily Millions* and gives players a chance to win $1,000 a week for life (ten year guarantee).

May 23 – *Wild Card* changes are introduced. The game is offered by Montana, Idaho and South Dakota.

1999

Scratch

- $ First product sold by the Montana Lottery. On June 24, 1987, Montana Lottery introduced Pot of Gold.
- $ Since 1987, over $114 million in Scratch tickets have been sold.
- $ Players remove latex covering over a play area.
- $ Play instructions are included on each ticket.
- $ In fiscal year 1999, Montana introduced 29 different games.
- $ Average Scratch ticket revenue per week was $140,666, for a total of $7,314,666.
- $ Prizes in fiscal year 1999 were $4,063,088, or 55% of revenue.
- $ Commissions to retailers of $548,233.

Powerball

- $ Introduced in April 1992 and redesigned in 1998.
- $ Currently operated in conjunction with twenty-one other lottery jurisdictions.
- $ Players pick five numbers from a field of 49, plus one number, the Powerball, from a field of 42 or they can play "Quick Pick" where the computer selects some or all of the numbers.
- $ Overall odds of winning are approximately 1:35.
- $ Odds of winning the jackpot are approximately 1:80 million.
- $ Nine ways to win prizes ranging from the jackpot to $3
- $ On March 27, 1999 Super 1 Foods in Kalispell sold a winning Powerball jackpot ticket to Dean Drenzek of East Glacier. The Drenzeks, schoolteachers in the Browning public schools, did not claim their prize until early June, waiting until school was out for the year to avoid disruption of their school and students.
- $ In fiscal year 1999, ten Montana Powerball players matched the five white balls but not the Powerball to collect the second tier $100,000 prize.
- $ Montana Powerball players played for a $250 million jackpot in July 1998. Over $1.2 million in Powerball sales for that draw.
- $ Players also played for a jackpot of $150 million on June 30, 1999. Over $540,000 in Powerball sales for that draw.
- $ Because of the two mega-million Powerball jackpot runs, Powerball sales ended 21% ahead of budget, and 20% ahead of Fiscal Year 1998 sales.
- $ Powerball revenue for the year totaled $14,578,227.
- $ Prizes in Powerball in fiscal year 1999 totaled $6, 879,066 or 47 percent of revenue.
- $ Commissions to retailers of $731,144.

Lottery Products

Montana Cash

- Introduced in May 1991.
- Players pick five numbers from a field of 37. "Quick Pick" option, where the computer picks the numbers, is also available.
- Overall odds of winning are approximately 1:43.
- Odds of winning the jackpot are approximately 1:217,949.
- Players can also win $200 for matching four of the five numbers, and $5 for matching three numbers.
- Montana Cash revenue for the year totaled $4,393,101.
- In fiscal year 1999, 18 players matched all five numbers to win or share jackpots ranging from $20,000 to $170,000.
- Prizes paid in Montana Cash in fiscal year 1999 totaled $2,206,038 or 50 percent of revenue.
- Montana Lottery retailers received $219,997 in commissions in fiscal year 1999.

Wild Card

- Played in Montana, Idaho and South Dakota.
- In fiscal year 1999, the game was redesigned to:
  - Make it easier to win
  - Give players two plays for $1
  - Give players the opportunity to select their own Wild Card
  - Improve the overall odds and the odds of winning the jackpot prize
- Players select five numbers out of 31, or they can "Quick Pick" where the computer selects the numbers. Players can also select or Quick Pick the Wild Card—a Jack, Queen, King or Ace from one of the four suits—Diamonds, Clubs, Hearts or Spades.
- In fiscal year 1999, one Montana player won the Wild Card Jackpot, $662,275.
- In fiscal year 1999, two players won $25,000.
- Other prizes include $5,000, $500, $20, $5, $2 and $1.
- Weekly sales averaged $52,535 for a total of $2,731,832.
- Prizes in fiscal year 1999 totaled $1,440,662, or 53% of revenue.
- Commissions to retailers of $136,657.

Cash 4 Life

- Played in Montana and ten other lottery jurisdictions.
- Players can win $1,000 a Week for Life.
- Other top prizes include $100,000, $50,000 and $25,000.
- Players win $1 for matching two numbers in a set of four.
- Players win $20 for matching three numbers in a set of four.
- In fiscal year 1999, one player won $25,000.
- Fifteen chances to win on each ticket.
- Weekly sales averaged $18,732, for a total of $974,074.
- Prizes in fiscal year 1999 totaled $461,622, or 47% of revenue.
- Commissions to retailers of $48,821.

August 27, 1999

To the Commissioners
Montana State Lottery
Helena, Montana

We have audited the accompanying financial statements of Montana State Lottery (Lottery), an enterprise fund of the State of Montana, as of and for the year ended June 30, 1999. These financial statements are the responsibility of the Lottery's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Lottery as of June 30, 1998 were audited by other auditors whose report dated September 3, 1998 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note A, the financial statements present only the Montana State Lottery and are not intended to present the financial position of the State of Montana and the results of its operations and cash flows of its proprietary fund types and non-expendable trust funds in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Montana State Lottery, an enterprise fund of the State of Montana, as of June 30, 1999, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

As discussed in Note P to the financial statements, the Lottery was required to change its fixed asset capitalization policy from $1,000 to $5,000 by the State of Montana during the fiscal year ended June 30, 1998.

In accordance with *Government Auditing Standards*, we have also issued a report dated August 27, 1999 on our consideration of the State of Montana's internal control over financial reporting as it relates to the Montana State Lottery and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

Galusha, Higgins & Galusha, PC

GALUSHA, HIGGINS AND GALUSHA, PC
Certified Public Accountants

Independent Auditor's Report

Balance Sheets
June 30,

ASSETS	1999	1998
CURRENT ASSETS		
Cash and cash equivalents	3,056,419	2,945,221
Accounts receivable, less allowance for doubtful receivables of $-0- in 1999 and $2,445 in 1998	1,751,681	950,975
Due from other funds	4,326	16,649
Inventory	744,266	314,447
Cash collateral - security lending transactions	161,905	194,340
Other current assets	33,669	47,492
Total current assets	5,752,266	4,469,124
PROPERTY, PLANT AND EQUIPMENT		
Furniture, fixtures and equipment	4,432,032	567,125
Accumulated depreciation	(577,547)	(395,821)
	3,854,485	171,304
INTANGIBLE ASSETS		
Software, net of accumulated amortization	1,108,929	
Other intangibles	5,985	13,246
	1,114,914	13,246
OTHER ASSETS		
Long-term receivable	2,014,421	1,880,647
	12,736,086	6,534,321
LIABILITIES AND FUND EQUITY		
CURRENT LIABILITIES		
Accounts payable	778,400	257,704
Estimated prize liability	1,527,180	1,447,023
Transfer obligations to general fund	2,842,718	2,259,184
Liability under security lending transactions	161,906	194,340
Due to other state agencies	80,754	61,681
Other current liabilities	74,671	142,425
Current portion of long term debt	905,482	
Total current liabilities	6,371,111	4,362,357
LONG-TERM LIABILITIES		
MUSL prize liability	1,830,143	1,755,908
Note payable	4,119,829	
Accrued compensated absences	177,320	178,373
	6,127,292	1,934,281
	12,498,403	6,296,638
FUND EQUITY		
Retained earnings	-0-	-0-
Contributed capital	237,683	237,683
	12,736,086	6,534,321

The accompanying notes are an integral part of these financial statements.

Balance Sheets

Statements of Revenues, Expenses & Changes in Retained Earnings
Year ended June 30,

	1999	1998
OPERATING REVENUES		
Instant ticket games	7,314,666	7,747,761
On-line games	22,677,234	22,027,399
Miscellaneous	83,744	86,329
Total operating revenues	30,075,644	29,861,489
COST OF TICKET REVENUES		
Instant ticket prize expense	4,063,088	4,628,726
On-line ticket prize expense	10,987,388	10,610,680
Retailer commission	1,684,852	1,731,700
On-line vendor fees	2,708,662	2,769,047
Cost of tickets sold	571,254	627,641
Total cost of ticket revenues	20,015,244	20,367,794
Net operating revenues	10,060,400	9,493,695
OPERATING EXPENSES		
Advertising	544,162	640,454
Other communications	138,693	137,796
Advertising production	134,221	131,433
Audit fees	42,843	35,354
Other contractual services	216,088	166,715
Depreciation and amortization	231,640	58,939
Management fees	119,569	117,119
Multi-state operating fees	84,284	101,277
Other	68,518	45,248
Personal services	1,240,582	1,290,089
Repairs and maintenance	55,396	50,067
Supplies and materials	132,884	161,110
Utilities and rent	95,844	95,186
Travel	31,910	25,795
Total operating expenses	3,136,634	3,056,582
OPERATING INCOME	6,923,766	6,437,113

The accompanying notes are an integral part of these financial statements.

Statements of Revenues, Expenses & Changes in Retained Earnings

Statements of Revenues, Expenses & Changes in Retained Earnings Continued
Year ended June 30,

	1999	1998
NON-OPERATING REVENUES (EXPENSES)		
Interest income	299,653	250,986
Interest expense	(46,456)	
Security lending income	10,804	6,125
Security lending costs	(10,295)	(5,975)
Gain on disposal of fixed assets	163	
Total non-operating revenues (expenses)	253,869	251,136
INCOME BEFORE OPERATING TRANSFERS	7,177,635	6,688,249
OPERATING TRANSFERS OUT		
General fund	6,780,404	6,569,565
Study of the Socioeconomic Impacts of Gambling Fund	47,231	52,708
Total operating transfers out	6,827,635	6,622,273
INCOME BEFORE CUMULATIVE AFFECT OF A CHANGE IN ACCOUNTING PRINCIPLE AND EXTRAORDINARY ITEM	350,000	65,976
CUMULATIVE EFFECT ON PRIOR YEARS OF ACCOUNT CHANGE		(65,976)
EXTRAORDINARY ITEM	(350,000)	
NET INCOME (LOSS)	-0-	-0-
Retained earnings, beginning of year		
Retained earnings, end of year	-0-	-0-

The accompanying notes are an integral part of these financial statements.

Statements of Revenues, Expenses & Changes in Retained Earnings, cont.

Statements of Cash Flows
Year ended June 30,

	1999	1998
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from sales	29,214,591	29,842,806
Cash paid to suppliers for goods and services	(6,800,502)	(6,835,260)
Cash paid to employees	(1,246,535)	(1,316,287)
Cash paid for prizes	(14,970,318)	(15,088,900)
Net cash provided by operating activities	6,197,236	6,602,359
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Operating transfers out:		
General fund	(6,196,870)	(6,051,756)
Study of Socioeconomic Impact of Gambling Fund	(47,231)	(52,708)
Net cash used by non-capital financing activities	(6,244,101)	(6,104,464)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase of fixed assets		(36,640)
Proceeds from sale of fixed assets	1,724	
Net cash provided (used) by capital and related financing activities	1,724	(36,640)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest income	155,830	250,986
Security lending income	10,804	6,125
Security lending costs	(10,295)	(5,975)
Net cash provided by investing activities	156,339	251,136
NET INCREASE IN CASH AND CASH EQUIVALENTS	111,198	712,391
Cash and cash equivalents, beginning of year	2,945,221	2,232,830
Cash and cash equivalents, end of year	3,056,419	2,945,221
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating income	6,923,766	6,437,113
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	231,640	58,939
Extraordinary loss	(350,000)	
Changes in assets and liabilities:		
Increase in accounts receivable	(800,706)	(28,871)
Decrease in due from other state agencies	12,323	
(Increase) decrease in inventory	(429,819)	187,017
(Increase) decrease in other current assets	13,823	(185,815)
Increase in long-term receivable	(133,774)	(34,631)
Interest receivable included in long-term receivable	143,824	
Decrease in other intangible assets	7,261	
Increase (decrease) in accounts payable	520,696	(125,113)
Interest expense included in accounts payable	(46,456)	
Increase in lottery prizes payable	154,392	134,030
Increase (decrease) in other current liabilities	(67,754)	130,520
Increase in due to other state agencies	19,073	
Increase (decrease) in compensated absences payable	(1,053)	29,170
Net cash provided by operating activities	6,197,236	6,602,359

Non cash transactions from capital and related financing activities in1999 consist of financing the cost of computer equipment and software through a long term note payable of $5,025,311 to Norwest Investment Services, Inc. There were no such activities in 1998.

The accompanying notes are an integral part of these financial statements.

Statements of Cash Flows

Note A - Summary of Significant Accounting Policies

Organization - The Montana State Lottery (hereafter referred to as the Lottery) was created in November 1986 by a referendum vote of the people of Montana. Section 23-7-101, Montana Code Annotated (MCA) establishes the provision of the code under which the Lottery operates. The Lottery is operated by a five-member commission consisting of Montana residents appointed by the Governor. The Commission, by law, has the power to operate a state lottery, determine the type and forms of lottery games, set ticket prices, determine the number and size of prizes, conduct lottery drawings, enter into agreements to offer lottery games with other states, and prepare financial reports. The Lottery is attached to the Montana Department of Commerce for administrative purposes.

Disposition of revenue is a minimum of 45 percent for prizes and a maximum of 10 percent for commission to sales agents. The remaining revenue, less operating expenses, is transferred to the Montana State General Fund. Section 23-7-401(5), MCA, states that for the purposes of funding a study of the socioeconomic impacts of gambling, $100,000 of Lottery net revenue may be appropriated during the biennium ending June 30, 1999. $47,231 and $52,708 of net revenue was utilized to fund the study during fiscal years 1999 and 1998, respectively, and is reflected in the financial statements as an operating transfer out.

Reporting Entity - The Lottery is included in the State of Montana's financial statements as an enterprise fund. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Lottery's financial statements as a reporting agency.

Basis of Accounting - The Lottery utilizes the accrual basis of accounting and is classified as an enterprise fund of the governmental proprietary fund type. Enterprise funds account for operations similar to private business enterprises where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or where the Legislature has decided that periodic determination of revenue earned, expenses incurred or net income is appropriate.

Revenue Recognition - Sales of instant lottery tickets are made to licensed retailers who market the tickets to the public on a commission basis. Revenue is recognized when tickets are activated by retailers. Tickets activated, but not sold by retailers, may be returned for credit. Sales are reduced for estimated ticket returns.

Sales of on-line lottery tickets are made to licensed retailers who market the tickets through the use of computerized terminals on a commission basis. Revenue is recognized on drawing dates. Tickets sold in advance of future drawing dates are recorded as deferred revenue until the ticket becomes valid for a drawing.

Cash and Cash Equivalents - Cash and cash equivalents consist of interest-bearing deposits with the Montana Board of Investments short-term investments pool, cash deposited with banks and cash on deposit with the Montana State Treasurer that is part of the State's pooled cash and is not separately identifiable as to specific types of securities. These funds are highly liquid and may be drawn on daily.

Inventory - Inventories consist of ticket and supplies. Ticket inventory includes instant lottery tickets that are carried at cost using the specific identification method. Tickets are charged to cost of sales when activated.

Unsold tickets are charged to cost of sales upon the end or cancellation of the related game. Supply inventory is carried at cost and expensed as used.

Prizes - Prize expense is recognized based on a predetermined prize structure for each instant ticket and on-line game. Free tickets are recorded as a reduction in revenue and not as prize expense.

Intangible Assets - Intangible assets consists of the following:
Software represents the amortized cost of software purchased in 1999. This software had an original cost of $1,150,000 and is being amortized over seven years.

Note A - Continued

Other intangibles represents the per ticket cost paid to Autotote Lottery Corporation for advance on-line ticket sales. These ticket sales, also referred to as deferred revenue, represent tickets sold prior to June 30, 1999 and 1998 for drawings held subsequent to year-end.

Fixed Assets - Fixed assets are recorded at cost. Donated fixed assets are recorded at their estimated fair market value at the date of donation. Ordinary maintenance and repairs are charged to operations as incurred; major renewals and betterments are capitalized. Upon disposition or retirement of fixed assets, the cost and related accumulated depreciation or amortization is removed from the accounts. Gain or loss on disposal is reflected in nonoperating revenues and expenses. Depreciation and amortization are calculated on a straight-line basis over estimated useful lives of two to ten years.

Contributed Capital - Contributed capital represents equity acquired through contributions from vendors and the State of Montana.

Compensated Absences - State employees earn vacation leave ranging from fifteen to twenty-four days per year based on years of service. Vacation leave may be accumulated to a total not to exceed twice the maximum number of days earned annually. Sick leave accumulates at a rate of twelve days per year with no maximum accumulation. Upon retirement or termination, an employee is paid for 100 percent of unused vacation leave and 25 percent of unused sick leave.

Reclassifications - Certain reclassifications have been made to the 1998 financial statements in order to conform to the 1999 presentation.

Note B - Cash and Cash Equivalents

Cash and cash equivalents consist of the following:

	June 30,	
	1999	1998
Short-term investment pool	$3,028,189	$2,901,850
Cash on deposit with State Treasurer	18,080	33,221
Cash in revolving deposit account	10,000	10,000
Petty cash	150	150
	$3,056,419	$2,945,221

The Montana State Lottery participates in the Montana Board of Investments Short Term Investment Pool (STIP). STIP balances are highly liquid investments with maturities of 397 days or less. There are no legal risks that the Board of Investments is aware of regarding any STIP investments. The bank balance of the revolving deposit account was $11,478 and $15,663 at June 30, 1999 and 1998, respectively, and was covered by federal depository insurance. The carrying amount reported in the balance sheet for cash and cash equivalents approximates the fair market value.

Note C - Other Current Assets

Other current assets consist of the following:

	June 30,	
	1999	1998
Prepaid expenses	$27,945	$42,442
Employee travel advances	5,724	5,050
	$33,669	$47,492

Note D - Fixed Assets

A summary of changes in fixed assets for the Montana Lottery for the year ended June 30, 1999 is as follows:

	Balance 6/30/98	Additions	Deletions	Balance 6/30/99
Equipment	$567,125	$3,875,311	$10,404	$4,432,032
Accumulated depreciation	$395,821	$ 190,569	$ 8,843	$ 577,547

Note E - Multi-State Lottery Association

Joint Venture Association - In November 1989, the Montana State Lottery joined the Multi-State Lottery Association (MUSL). MUSL was created in September 1987 to operate a multi-state lottery game for the benefit of party lotteries. The Lotto*America/ Powerball game, Wild Card game and Cash 4 Life game are presently the only games operated jointly by the members. Each lottery participating in MUSL is represented on the Board of Directors.

Prize Reserve Fund Receivable/Payable - As a member of the MUSL, the Lottery is required to contribute to various prize reserve funds maintained by MUSL. The contributions are to be used to fund unanticipated prize claims. All funds remitted and the related interest earnings will be returned to the Lottery upon leaving the association, less any portion of unanticipated prize claims, which may have been paid from the fund.

The Lottery contributes to the reserve fund through the set-aside for prizes. Payments made to the reserve fund are considered a portion of the prize expense associated with the on-line game.

During 1990, the MUSL Board created the unreserved accounts to record interest earned on the various prize reserve funds when the prize reserve fund balance is not below the predetermined ceiling amount. The amounts in the unreserved accounts may be used at the Board's discretion.

The long-term receivable balance of $2,014,421 and $1,880,647 at June 30, 1999 and 1998, respectively, represents the Lottery's share of the MUSL prize reserve fund that had a balance of $97,269,759 and $94,131,232 for 1999 and 1998, respectively. The long-term liability balance of $1,830,143 and $1,755,908 at June 30, 1999 and 1998, respectively, represents the Lottery's share of the total estimated prize liability.

Lotto*America Prizes and Investments - Prizes awarded to Lotto*America grand prize winners are paid in twenty annual installments funded by investments in United States Treasury zero coupon bonds. Bonds purchased on behalf of Montana source winners are held in trust by MUSL with the Montana State Lottery as beneficiary. As the bonds mature, the proceeds are forwarded to the Montana State Lottery and distributed to the grand prize winners on the anniversary date of each win.

At June 30, 1999 and 1998, MUSL held United States Government zero coupon bonds in trust for the Montana State Lottery winners with respective par values of $70,789,948 and $75,997,948 and respective market values of $47,272,236 and $51,878,911.

The Montana State Lottery has eight Lotto*America/Powerball/Tri-West winners. The combined total future prize payments owed is $70,789,000 and $75,997,000 at June 30, 1999 and 1998, respectively. Total annual payments due over each of the next five years is $5,208,000 annually and $44,749,000 thereafter. The present value of future prize payments approximates the current market value of the bonds held in trust for the Montana State Lottery winners.

Note E - Continued

Multi-State Lottery Association Financial Position - Information related to the Multi-State Lottery Association's audited financial statements is as follows:

	June 30, 1999	June 30, 1998
Total assets	$1,585,325,696	$1,655,688,518
Total liabilities	1,585,096,945	1,655,424,985
Total net assets	228,751	263,533
Total liabilities and net assets, unrestricted	$1,585,325,696	$1,655,688,518
Total revenues	$ 2,713,805	$ 3,123,770
Total expenses	2,748,587	3,151,567
Decrease in unrestricted net assets	$ (34,782)	$ (27,797)

Note F - Estimated Prize Liability

The estimated prize liability represents the Lottery's estimate of prizes payable related to games in process at year-end based on the predetermined prize structure of each outstanding game.

Note G - Obligation to Transfer Funds

The Montana State Lottery is required to transfer its net revenue to the Montana State General Fund. This change was enacted through the passage of SB 83 by the 1995 Legislature and signed into law by Governor Racicot in April 1995. Transfer obligations outstanding at June 30, 1999 and 1998 were $2,842,718 and $2,259,184, respectively.

Note H - Other Current Liabilities

Other current liabilities consist of the following:

	June 30, 1999	June 30, 1998
Property held in trust	$ 3,000	
Deferred on-line revenue	71,671	$142,425
	$74,671	$142,425

Note I - Long-Term Liabilities

Long-term liabilities consist of the following:

	June 30, Current	Long-Term	1999 Total	1998 Total
Prize liability Multi-State Lottery Association		$1,830,143	$1,830,143	$1,755,908
Accrued compensated absences		177,320	177,320	178,373
Note payable - Norwest Investment, interest rate 5.12% for 5 years requiring quarterly payments of $286,394.30.	$905,482	4,119,829	5,025,311	
	$905,482	$6,127,292	$7,032,774	$1,934,281

Future scheduled maturities of the long term note payable are as follows:

2000	$ 905,482
2001	952,741
2002	1,002,466
2003	1,054,786
2004	1,109,836
Total	$5,025,311

Note J - Leases

The Lottery leases its office, administrative and warehouse facilities under a lease agreement expiring February 2002. Rent expense under operating leases charged to operations was $78,000 for the years ended June 30, 1999 and 1998.

Note K - Contributed Capital

Contributed capital decreased $1,360 during 1998. The decrease is related to the State of Montana changing its fixed asset capitalization policy from $1,000 to $5,000.

Note L - Employee Benefit Plans

Pension Plan - The Lottery participates in the Public Employees Retirement System (PERS). PERS is a statewide mandatory cost-sharing multiple employer defined benefit retirement plan which covers all employees. The plan is established under State law and is administered by the State of Montana. The plan provides retirement, disability, and death benefits to plan members and beneficiaries.

The plan issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained from the following address: Public Employees Retirement System, Public Employees Retirement Division, P.O. Box 200131, 1712 Ninth Avenue, Helena, MT 59620-0131, (406) 444-3154.

Contribution rates for the plan are required and determined by State law. The contribution for 1998, expressed as a percentage of covered payroll, was 6.8% for the employer. Effective July 1, 1997, the contribution rate for 1998, expressed as a percentage of covered payroll, increased from 6.7% to 6.8% for employees.

The amounts contributed to the plan during the years ended June 30, 1999, 1998 and 1997, were $127,111, $129,256 and $115,558, respectively, and were equal to the required contributions for each year.

Deferred Compensation Plan - The Lottery's permanent employees are eligible to participate in the State of Montana's deferred compensation plan. The plan is administered by Benefits Corporation on behalf of Great West Life Insurance Company through a contract with the State of Montana. The amount of compensation deferred is not available to employees until termination, retirement, death, or unforseen emergency. All amounts deferred under the plan created under Internal Revenue Code Section 457 remain the property of the State of Montana until paid, subject only to claims of the State of Montana's general creditors. Participants' rights under the plan are equal to those of general creditors of the State of Montana in an amount equal to the fair market value of the deferred account for each participant.

Note M - Related Party Transactions

During the ordinary course of business, other State agencies provide certain services and supplies to the Lottery. During 1999 and 1998, total payments to other State agencies were approximately $326,000 and $313,000, respectively.

Note N - Commitments and Contingencies

Instant Tickets - The Lottery has an agreement with BABN Technologies Corporation to print instant game tickets. The agreement expires June 30, 2001.

Maintenance Contract - The Lottery has an agreement with Stratus Computer, Inc. to provide for computer hardware and software maintenance. The agreement provides for quarterly payments of $9,587. The agreement may be canceled by either party with proper notification.

On-line Vendor - Lottery is contracted with Autotote Lottery Corporation to provide for the operation of an on-line gaming system through March 30, 2006. The estimated total contract price is approximately $24 million over the seven year contract.

Advertising - The Lottery signed a contract with Banik & Associates to provide advertising services for $8,400 per month through December 1999.

Independent Observation of Drawings - Lottery is committed to Henry Fenton, CPA, to observe Montana Cash and other special drawings. The term of the contract is for one year ending June 30, 2000. Compensation will not exceed $8,000.

Prize Contingencies - Certain Big Spin prizes awarded are payable to the winners in annual installments spanning seventeen to twenty years with the first payment being made by the Lottery.

Note N - Continued

The Lottery has entered into agreements with an insurance carrier under which purchased annuities will provide the required level of payments corresponding to the Lottery's obligation to these prize winners. Because it is the intent of the Lottery that the insurance carrier will make future installment payments directly to each prize winner, neither the present value of the annuities nor the present value of the future payments are reflected in the accompanying financial statements. The Lottery would be liable for such future payments in the gross amount of $1,984,559 and $2,234,559 at June 30, 1999 and 1998, respectively, if the insurance carrier defaulted on their payments.

Litigation - The Lottery is involved in one legal action arising in the normal course of business. The Lottery intends to vigorously defend this action. In the opinion of management and legal counsel, such matters will not have a material effect upon the financial position or results of operations of the Lottery.

Note O - Extraordinary Item

The Montana Lottery awarded a seven-year contract to Autotote Lottery Corporation (ALC) for the implementation and operation of an on-line lottery system. Automated Wagering International (AWI), who also bid on the contract, contested the award of the contract to ALC. The protest by AWI was settled by the Montana Lottery, ALC and AWI in a settlement agreement dated February 1999. The agreement required a $500,000 payment to AWI to discharge and release all parties from any further action related to the protest. The settlement dictated that ALC contribute $150,000 to the Montana Lottery to be applied to the Montana Lottery's required $500,000 payment to AWI. $350,000 was paid to AWI from Lottery funds on February 26, 1999, and $150,000 was paid on June 25, 1999.

Note P - Cumulative Effect on Prior Years of Accounting Change

Effective July 1, 1997, the Lottery was required to change its fixed asset capitalization policy from $1,000 to $5,000 by the State of Montana. This change in accounting principle resulted in a charge to net income of $65,976 for the year ended June 30, 1998.

Note Q - Risk Management/Public Entity Risk Pool

The Montana State Lottery contributes to the Group Employee Comprehensive Medical and Dental Plan and the Property and Casualty Insurance plans of the State of Montana. Details of these plans can be found in the State of Montana Comprehensive Annual Financial Report.

Note R - Reconciliation to the Montana Comprehensive Annual Financial Report

In order to create financial statements that are more useful for users of the Montana State Lottery's financial statements, the classification of some items in the Lottery financial statements differ from the Montana Comprehensive Annual Financial Report (CAFR). The following is a reconciliation of these items.

Lottery statements:	
Lottery Operating Transfer Out	$47,231
CAFR:	
Operating Transfer Out	45,000
Amounts included in expense categories:	
Contracted services	808
Supplies and materials	26
Communication	455
Travel	942
Total	$47,231

Note S - Reclassifications

Certain accounts in the prior year financial statements have been reclassified for comparative purposes to conform with the presentation in the current year financial statements.

Note T - Advertising Costs

Advertising costs are expensed in the year they are incurred.

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